

Before the
UNITED STATES COPYRIGHT ROYALTY JUDGES
LIBRARY OF CONGRESS
Washington, D.C.

In the Matter of:

DETERMINATION OF RATES
AND TERMS FOR MAKING AND
DISTRIBUTING PHONORECORDS
(PHONORECORDS III)

Docket No. 16-CRB-0003-PR
(2018-2022)

**COPYRIGHT OWNERS' RESPONSE
TO THE SERVICES' JOINT MOTION FOR
REHEARING TO CLARIFY THE REGULATIONS**

PRYOR CASHMAN LLP

Donald S. Zakarin
James A. Janowitz
Frank P. Scibilia
Lisa M. Buckley
Benjamin K. Semel
7 Times Square
New York, New York 10036
Tel.: 212-421-4100
dzakarin@pryorcashman.com
jjanowitz@pryorcashman.com
fscibilia@pryorcashman.com
lbuckley@pryorcashman.com
bsemel@pryorcashman.com

Counsel for Copyright Owners

The National Music Publishers' Association ("NMPA") and the Nashville Songwriters Association International ("NSAI") (the "Copyright Owners") submit this response to the Services' Joint Motion for Rehearing to Clarify the Regulations (the "Joint Service Motion" or "JSM"). The Copyright Owners agree that certain of the regulatory terms ("Regulatory Terms") attached to the Initial Determination (the "Determination") should be clarified and/or modified and have proposed their own clarifications. Certain of the proposed changes in the JSM are acceptable to the Copyright Owners, and the lack of objection is noted below.¹ Other proposed changes in the JSM are not consistent with the Determination and should not be adopted.

ARGUMENT²

I. Typographical and Clerical Errors

A. Table of Contents

The Copyright Owners agree that the Table of Contents should accurately reflect the final section headings in the Regulatory Terms.³

B. Paragraph Numbering

The JSM proposes typographical fixes to paragraph numbering in the definition of Free Trial Offering. The Copyright Owners agree with the goal of simplifying the Regulatory Terms, as explained in Section I of their Motion For Clarification or Correction of Typographical Errors and Certain Regulatory Terms ("Motion for Clarification"), but believe that a roll forward of promotional offering allowances is best accomplished by adopting the current Section 385.14 in

¹ The Copyright Owners and the Services reached agreement on certain additional clarifications, as set forth in the joint stipulation at Attachment A hereto.

² For simplicity, this response follows the numbering of the sections in the JSM, repeating each JSM section heading and then inserting a response.

³ Since the Copyright Owners submit that the full text of the current Section 385.14 provision addressing the complex scope of accepted Promotional Offerings should be included in the Regulatory Terms, the Copyright Owners' Table of Contents is different from that proposed by the Joint Service Motion, in that the Copyright Owners' proposal has one additional section (corresponding to such Promotional Offerings).

whole, and that this section should replace the split and overlapping definitions of Promotional and Free Trial Offerings in the Regulatory Terms. Free Trial Offering would thus not be a separately defined term.

C. Cross References

The Copyright Owners do not object to the JSM proposal to correct the cross-reference in §385.4. Other cross references are addressed by the separate sections below.

D. Other Typographical Corrections

With respect to the double negative in the Promotional Offering definition noted in the JSM, the Copyright Owners submit that their proposed definition of Promotional Offering in the Motion for Clarification is consistent with the Determination, and avoids the double negative.

II. Definitional Issues

A. Certain Defined Terms Are Not Used

The JSM proposes that defined terms be capitalized and the Copyright Owners have no objection to doing so.

B. Certain Capitalized Terms Are Used But Not Defined

While Copyright Owners agree with capitalizing defined terms, they submit that the term “Service” should be defined in the Regulatory Terms, as discussed in Section A of the Motion for Clarification. On the other hand, the term “Free Trial Offering” should not be separately defined, as it is properly covered by the current Promotional Offering terms embodied in §385.14.

C. Clarification of Certain Definitions

1. Definition of Licensed Activity

The JSM agrees with Section B of the Motion for Clarification that former Subpart A products (“physical phonorecords, Permanent Digital Downloads, Ringtones”) should not be included in the definition of Licensed Activity. However, the JSM further qualifies the definition

so it only includes “musical works subject to Subparts C and D of this title, and licensed pursuant to 17 U.S.C. 115.” This additional provision would result in a change to the way royalties are calculated that is not supported by the evidentiary record and is not consistent with the Determination. The Judges should therefore reject this provision.

The intended effect of this proposed amendment appears to be to carve out direct licensing deals from the definition – but that is improper and confuses how the defined term Licensed Activity is used in the Regulatory Terms. In Step 3 of §385.21, Licensed Activity is used to define the scope of the total payable royalty pool from which royalties are then allocated to individual works (in step 4). The Step 3 payable royalty pool is, and must be, the amounts payable from all streaming activity. Then, once the Step 4 per-work allocation/calculation is made, the per-work royalty so calculated is only due for those works for which compulsory licenses have been obtained (*i.e.*, not works under direct deals). Those works subject to direct deals will have their own payable royalty pool, which will be allocated in accordance with the specific terms of each deal.

Section 385.21(a) already expressly limits its mandate to pay statutorily allocated royalties to “Licensed Activity covered by this Subpart pursuant to 17 U.S.C. 115” (emphasis added). This limitation addresses any concern about direct deals being overridden by statutory rates. The royalty calculations of Subpart C do not work if the limitation is also baked into the definition of Licensed Activity itself because the Step 4 calculation of which royalties are payable for works licensed under the Section 115 compulsory license requires the inclusion of all streaming activity involved in an Offering in order to make the per song/per stream allocation required by Step 4.

2. *Definition of “Offering”*

The JSM also agrees with Section B of the Copyright Owner’s Motion for Clarification that former Subpart A products (“physical phonorecords, Permanent Digital Downloads, Ringtones”) should not be included in the definition of Offering.

The JSM's proposed additional edits to the definition of Offering suffer from a similar problem as that discussed above with respect to Licensed Activity to the extent that it seeks to limit Offering to activity "licensed under 17 USC 115 and subject to Subparts C or D of this title, including Incidental Deliveries of embodiments of musical works." This provision would also result in a change to the way royalties are calculated that is not supported by the evidentiary record and is inconsistent with the Determination. While the Services claim that the Judges' definition would be confusing, their proposed modification would be more confusing.⁴ The definition of Offering propounded by the Copyright Owners in their Motion for Clarification suffers from none of these issues.⁵

Offering is used to capture the products offered to End Users that entail Licensed Activity. For example, subscription service is defined as "a digital music Offering for which End Users are required to pay a fee to have access to the Offering." And Service Revenue is defined as including "[a]ll revenue from End Users recognized by a Service for the provision of any Offering." As with "Licensed Activity, "Offering" is also a part of the determination of the payable royalty pool in §385.21. "Offering" therefore must not be limited to only activity for which a compulsory license has been obtained. Where a Service provides a subscription streaming service to End Users, and a portion of the musical works streamed via this service are licensed under direct deals, the compulsory per work royalty cannot be computed unless the payable royalty pool first includes all works so that the per work royalty payable for works licensed under the compulsory license can be properly allocated.

⁴ As the definition of "Incidental Deliveries" provides, they are copies made to facilitate the streams that are offered to End Users and hence are not themselves "Offerings." The Services' inclusion of "Incidental Deliveries" in the definition of "Offering" can therefore create confusion, as the Services do not separately offer Incidental Deliveries to End Users.

⁵ The Copyright Owners again propose the following definition: "Offering means a Service's engagement in Licensed Activity." Exh. B, p. 6.

Again, the exclusion of payments for works covered under direct deals, which are not subject to the royalty computations in Section 385.21 (unless a direct license so provides) is addressed in the allocation phase of the royalty calculation, where the determined per-work royalty applies only to works for which a compulsory license under Section 115 is obtained, while royalty payments for works licensed under direct deals remain to be determined by the payment terms in those deals.

To be clear, works licensed under direct deals cannot be excluded from the definition of “Licensed Activity” or “Offering” because the total payable royalty pool in §385.21 has to be allocated based on the percentage of works and streams licensed under Section 115 as compared to those licensed directly. That allocation cannot be done unless all works and all streams, both those subject to compulsory license and those directly licensed, are initially included.

3. *Definition of “Performance Royalty”*

The joint stipulation as to this term is set forth in Attachment A hereto.

4. *Definition of “Play”*

The joint stipulation as to this term is set forth in Attachment A hereto.

5. *Definition of “Fraudulent Stream”*

The JSM’s proposed edit to Fraudulent Stream is to use Play in the definition instead of Stream, thus capturing potentially fraudulent plays of limited downloads as well as streams. This raises an issue that should also be clarified in the Regulatory Terms. Does 50 “straight” plays include a situation where a track is played by limited download 50 straight times, even where there may be interactive streams of other tracks interspersed? The Services’ definition also invites them to unilaterally exercise discretion in making a determination as to whether the “Play” was “not initiated or requested by a human user” and hence omit all such uses from royalty calculations.

To cabin such unilateral discretion and to aid in the resolution of disputes, the Copyright Owners submit that, in addition to the edit proposed by the Services to Fraudulent Stream, the Recordkeeping section be clarified to ensure that records are kept of Fraudulent Streams that are omitted from royalty calculations in the same way as records of other “zero rate” uses. This would not require Services to track something that they will not already be tracking (as they will already need to track streams they claim are fraudulent to exclude them from the royalty calculation); it would merely require them to maintain those records. The clarification can be accomplished by merely adding three words to Section 385.4(b), so that it begins: “The Service claiming zero rates or Fraudulent Streams shall maintain the records required by this section...”, and to Section 385.4(c), so that it reads: “If a Copyright Owner or agent requests information concerning zero rate Offerings or Fraudulent Streams, the Licensee shall respond to the request within an agreed, reasonable time.”

6. *Definition of “Locker Service”*

The Copyright Owners agree with fixing the typographical error in this definition. However, as discussed in Section H of the Motion for Clarification, there are additional points that need to be clarified in this definition, and in the related definition of Purchased Content Locker Service. Moreover, as discussed in Section A of the Motion for Clarification, the Copyright Owners believe that it is important to define the term “Service” in the Regulatory Terms.

7. *Definition of “Family Plan or Family Account”*

The Copyright Owners vigorously disagree with the Services’ proposal to remove the word “discounted” from the definition of Family Plan or Family Account. It would gut the provision and enable the Services to pay Copyright Owners based on 1.5 times an individual subscription rate while charging higher rates to Families.

The Determination explicitly bases its allowance of discounts to the mechanical floor for family and student plans on the allegations by the Services that these plans serve customers with low willingness to pay (WTP).⁶ Despite the overwhelming evidence at the hearing that this was in fact not the reason for such plans, which were instead targeted at obtaining long-term and high-value customers (to wit, college students and families can obtain discounts, but not the working youth or senior citizens), the Determination put faith in the Services' unsupported claims that they were targeting low-WTP groups and allowed for discounts to the mechanical floors for these "discounted service users" (*e.g.*, Determination at 90).

Now the Services seek to remove the "discounted" requirement for which they argued so strenuously, which would allow them to sell subscriptions to these high-value groups even at higher or full rates while paying at a reduced royalty rate to the Copyright Owners. That was not the reasoning in the Determination for accepting these discounted plans.

In setting a Family Plan subscriber at 1.5 subscribers for purposes of the mechanical floor, the Determination referred to the fact that "[t]he Services presented evidence of three subscription variations: discounted annual subscriptions, family subscriptions, and student subscriptions." (Determination at 93) Indeed, the Services presented evidence exclusively of a single family plan pricing model – namely, 1.5 times the individual subscription price - \$15 versus \$10.

This is the Family Plan model that underlies the Determination's 1.5x subscriber adjustment. Having obtained what they sought, the Services now want to remove "discounted" altogether. It is entirely improper for the Services to obtain authority to limit royalties for discounted plans while jettisoning the requirement that the plans be discounted. At a minimum, the 1.5x subscriber Family Plan mechanical floor cap should require that the Services charge no

⁶ The Copyright Owners continue to request that the definition of Student Plan be clarified in the manner set forth in Section E of their Motion for Clarification.

more than 1.5x individual subscription price. If they do, the 1.5x cap should correspondingly go up as well.

Furthermore, both Amazon's and Pandora's proposed rates and terms included the standard limit of 6 people under the definition of a Family Plan. It is appropriate therefore that the limit of 6 people in the family plan should be retained, which Copyright Owners believe was intended by the Judges in the Determination.

The Copyright Owners thus submit that the Services' proposed removal of the word "discounted" should be accompanied by the inclusion of a more precise provision as follows:

Family Plan or Family means an ~~discounted~~ Offering to be shared by ~~two or more~~ up to six family members for a single subscription price that is no more than 1.5 times the individual subscription price for the Offering.⁷

The approach above, as modified by footnote 6's proportionate increase for rate increases charged by the Services, is consistent with language proposed by Google in its initial Proposed Rates and Terms:

The per-subscriber minima applicable to Family Plans shall be calculated by multiplying the applicable minimum by the ratio of the Family Plan price to the individual subscription price.

Google Inc.'s Proposed Terms (submitted with its Written Direct Statement), §385.23. Google's proposal did not, however, expressly include the 1.5x floor (although it was presumably intended given that the Services all proposed a 1.5x subscription price for Family Plans).

Regardless of which approach is taken by the Judges, the reasoning for allowing a Family Plan cap to the mechanical floor was that it was mirrored by a like discount in prices for Family Plans. Paying on a discounted basis without the discount – just a further revenue displacement gambit – is not what the reasoning in the Determination reflects.

⁷ To the extent that the Services want the ability to charge more than 1.5x the individual subscription price for Family Plans, the mechanical floor should be calculated using the ratio of the price of the Family Plan to the individual plan.

8. *Use of “Family Plan End User”*

The joint stipulation as to this term is set forth in Attachment A hereto.

9. *“Due Date” Not Defined in Section 385.3*

The modification proposed by the Services to the late fee provision of Section 385.3 is unnecessary and confusing. The Services seek to make specific cross-reference to the applicability of Part 210, and to repeat only some of the language therein. Part 210 applies to all compulsory royalty payments, and addresses due dates and the payment of agents of copyright owners. But selectively invoking one portion of Part 210 for Section 385.3 and not for all of the other royalty provisions to which Part 210 equally applies (and only invoking part but not all of Part 210) could be interpreted as excluding application of other parts of Part 210. The change is unnecessary and confusing.

III. Other Proposed Changes

Finally, the Services attach to the JSM a redline of the Regulatory Terms in which they propose numerous changes that are nowhere discussed in the JSM. Contrary to the Service’s statement that those changes are merely “typographical and clerical corrections” (JSM at 2), many of these changes are, in fact, substantive. The Judges should not adopt any of the changes proposed in the Services’ redlined Regulatory Terms for which the Services have presented no argument or rational in the JSM.

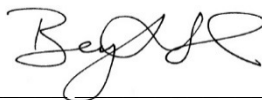
One such change in particular is worth noting. In the definition of “Service Revenue,” the Services propose to add the phrase “in connection with an Offering” to subpart (3). This is improper because subpart (3) covers Bundles, and Bundles include products or services that are not Licensed Activities. The proposed change would permit the Services to determine that some

portion of the advertising or sponsorship revenue associated with the Bundles was not made “in connection with an Offering” and exclude that revenue.⁸

Dated: March 5, 2018

Respectfully submitted,

PRYOR CASHMAN LLP

By: _____

Donald S. Zakarin
James A. Janowitz
Frank P. Scibilia
Lisa M. Buckley
Benjamin K. Semel

7 Times Square
New York, New York 10036
Tel.: 212-421-4100
dzakarin@pryorcashman.com
jjanowitz@pryorcashman.com
fscibilia@pryorcashman.com
lbuckley@pryorcashman.com
bsemel@pryorcashman.com

Counsel for Copyright Owners

⁸ The Copyright Owners further continue to believe that subpart (5) should be clarified in the manner discussed in Section J of their Motion for Clarification.

Attachment A

Pursuant to the direction in the February 21, 2018 scheduling order issued by the Copyright Royalty Judges, the National Music Publishers' Association ("NMPA"), the Nashville Songwriters Association International ("NSAI" and together with the NMPA, the "Copyright Owners"), Amazon Digital Services LLC ("Amazon"), Google Inc. ("Google"), Pandora Media, Inc. ("Pandora"), and Spotify USA Inc. ("Spotify" and together with Amazon, Google and Pandora, the "Services") (the Copyright Owners and the Services collectively, the "Moving Parties") have met and conferred through counsel with respect to areas of potential agreement regarding changes to the regulations attached to the Initial Determination the Copyright Royalty Judges issued on January 27, 2018. While the Moving Parties were not able to reach an agreement on every issue raised in their respective motions, agreement was reached on the following issues, which the Moving Parties respectfully request the Copyright Royalty Judges adopt as part of any revised regulations issued after the Copyright Royalty Judges have ruled on the Moving Parties' respective motions.

The Definition of Play

The Copyright Owners and the Services each sought modifications to the definition of Play contained in Section 385.2 to clarify how the definition would apply to tracks of less than 30 seconds in duration. The Moving Parties respectfully request that the Copyright Royalty Judges adopt the following definition, which the Moving Parties believe addresses their respective concerns in a manner consistent with the Initial Determination:

Play means (1) with respect to a track that lasts in its entirety 30 seconds or more, an Interactive Stream or play of a Limited Download of 30 seconds or

more and (2) with respect to a track that lasts in its entirety under 30 seconds, an Interactive Stream or play of a Limited Download of the entire duration of the track. A Play excludes Fraudulent Streams.

Family Plan Proration

The Copyright Owners and the Services each sought modifications to the provision in Section 385.22(b) addressing how a Family Plan subscription should be prorated for a partial month. In particular, the regulation¹ referenced an “end user,” but a Family Plan by its nature has multiple individual end users. The Moving Parties respectfully request that the Copyright Royalty Judges adopt language for this family plan proration provision clarifying that it shall be:

...prorated in the case of a Family Plan account that subscribed for only part of a calendar month.

The Moving Parties believe this addresses their respective concerns in a manner consistent with the Initial Determination.

The Definitions of Applicable Consideration and Performance Royalties

The Copyright Owners sought to add a definition of “Applicable Consideration” to the regulations, which the Copyright Owners argued was inadvertently omitted. The Services’ motion did not address this omission. The Services sought to delete the definition of “Performance Royalties,” which the Services argued was not used and that, if used, would incorrectly exclude a large portion of the performance royalties actually paid by the Services. The Copyright Owners’ motion did not address the definition of Performance Royalties.

As part of a compromise between the Moving Parties, the Copyright Owners have agreed that the Copyright Royalty Board should delete the definition of Performance Royalties and the

¹ For reference, the sentence in question is “A Family plan shall be treated as 1.5 subscribers per month, prorated in the case of a Family plan end user who subscribed for only part of a calendar month.”

Services have agreed that the Copyright Royalty Board should add a definition of Applicable Consideration. Accordingly, the Moving Parties respectfully request that the Copyright Royalty Judges make the following changes to the regulations:

Delete the definition of “Performance Royalty” in Section 385.2.

Add the following definition to Section 385.2:

***Applicable Consideration* means anything of value given for the identified rights to undertake the Licensed Activity, including, without limitation, ownership equity, monetary advances, barter or any other monetary and/or nonmonetary consideration, whether such consideration is conveyed via a single agreement, multiple agreements and/or agreements that do not themselves authorize the Licensed Activity but nevertheless provide consideration for the identified rights to undertake the Licensed Activity, and including any such value given to an affiliate of a record company for such rights to undertake the Licensed Activity. For the avoidance of doubt, value given to a copyright owner of musical works that is controlling, controlled by, or under common control with a record company for rights to undertake the Licensed Activity shall not be considered value given to the record company. Notwithstanding the foregoing, applicable consideration shall not include in-kind promotional consideration given to a record company (or affiliate thereof) that is used to promote the sale or paid use of sound recordings embodying musical works or the paid use of music services through which sound recordings embodying musical works are available where such in-kind promotional consideration is given in connection with a use that qualifies for licensing under 17 U.S.C. 115.**

Because these proposed changes were agreed by the Moving Parties as part of a compromise, the Moving Parties respectfully request that if the Copyright Royalty Judges are inclined to enter one of these changes, but not the other, the applicable party be given the opportunity to submit further written argument addressing the other party’s proposed changes.

Certificate of Service

I hereby certify that on Monday, March 05, 2018 I provided a true and correct copy of the Copyright Owners' Response to Services' Joint Motion for Rehearing to the following:

Pandora Media, Inc., represented by Meredith I Santana served via Electronic Service at meredith.santana@weil.com

Amazon Digital Services, LLC, represented by Michael S Elkin served via Electronic Service at MElkin@winston.com

Spotify USA Inc., represented by Richard M Assmus served via Electronic Service at rassmus@mayerbrown.com

Johnson, George, represented by George D Johnson served via Electronic Service at george@georgejohnson.com

Apple Inc., represented by Phil L. Hill served via Electronic Service at phil.hill@kirkland.com

Google Inc., represented by Katherine Merk served via Electronic Service at kmerk@kslaw.com

Signed: /s/ Benjamin K Semel